

**UNITED STATES DISTRICT COURT  
DISTRICT OF NEVADA**

YAMAGATA ENTERPRISES, INC., et al.,  
vs.  
GULF INSURANCE COMPANY, et al.,  
Plaintiffs,  
Defendants.

Case No. 2:07-cv-00644-HDM-GWF

## ORDER

## **Motion to Bifurcate Bad Faith Claims and Stay Discovery - #30**

This matter is before the Court on Defendant The Travelers Indemnity Company's Motion to Bifurcate Bad Faith Claims, and Stay Discovery Related to Bad Faith Claims Pending Resolution of Contingent Contract Claims (#30), filed on November 15, 2007; Plaintiffs' Response to Defendants' Motion to Bifurcate Bad Faith Claims, and Stay Discovery Related to Bad Faith Claims Pending Resolution of Contingent Contract Claims (#36), filed December 3, 2007; and Defendant The Travelers Indemnity Company's Reply to Plaintiffs' Opposition to Motion to Bifurcate Bad Faith Claims, and Stay Discovery Related to Bad Faith Claims Pending Resolution of Contingent Contract Claims (#38), filed December 17, 2007. The Court conducted a hearing in this matter on December 21, 2007.

## DISCUSSION

This case involves claims by Plaintiffs for breach of contract, declaratory judgment, breach of the implied covenant of good faith and fair dealing (“insurance bad faith”) and violation of Nevada Unfair Claims Practices Act, NRS 686A.310 against Defendants Gulf Insurance Company and Travelers Indemnity Company (hereinafter collectively referred to as “Travelers”). The factual

1 allegations and legal issues involved in this case are more fully discussed in the Court's order regarding  
 2 Plaintiffs' Motion to Compel and For Sanctions (#28). Travelers moves the Court to bifurcate trial of  
 3 Plaintiffs' breach of contract and declaratory judgment claims from their insurance bad faith and  
 4 statutory violation claims and to stay discovery on the latter claims until the coverage issues are  
 5 resolved.

6 Pursuant to Fed.R.Civ.Pro. 42(b), the court, in furtherance of convenience and to avoid  
 7 prejudice, or when separate trials will be conducive to expedition and economy, may order separate  
 8 trials of any claims or issues. The Court has broad discretion under Rule 42(b) to bifurcate the trial of  
 9 claims or issues, thereby deferring costly and possibly unnecessary proceedings pending resolution of  
 10 dispositive claims or issues. *Zivkoviv v. Southern California Edison Co.*, 302 F.3d 1080, 1088 (9<sup>th</sup> Cir.  
 11 2002). The court, in its discretion, may also bifurcate and stay discovery on the claims or issues to be  
 12 tried in the second phase of the case, depending on the outcome of the first phase of the trial. *Ellingson*  
 13 *Timber Co. v. Great Northern R.R. Co.*, 424 F.2d 497, 499 (9<sup>th</sup> Cir. 1970).

14 Bifurcation of the trial of insurance coverage and bad faith claims is often warranted for reasons  
 15 of convenience, expedition and judicial economy and also to avoid prejudice to either party, but  
 16 particularly to the defendant insurance company. Under Nevada law, insurance bad faith claims are not  
 17 *per se* legally premature because they are brought prior to the resolution of the insurance coverage  
 18 dispute. *Miles v. State Farm Mutual Automobile Ins. Co.*, 27 F.Supp.2d 1246, 1247 (D.Nev. 1998);  
 19 *Drennan v. Maryland Casualty Co.*, 366 F.Supp.2d 1002, 1005-1006 (D.Nev. 2005). *Drennan* notes  
 20 that an insured is not required to demonstrate that he is entitled to a directed verdict on the contractual  
 21 claim to establish a *prima facie* bad faith claim. *Id.*, 366 F.Supp.2d at 1006, *citing Albert H. Wohlers &*  
 22 *Co. v. Bartgis*, 114 Nev. 1249, 969 P.2d 949, 955 n. 2 (1999). In order to prove insurance bad faith,  
 23 however, the plaintiff must establish that the insurer had no reasonable basis for disputing coverage and  
 24 that the insurer knew or recklessly disregarded the fact that there was no reasonable basis for disputing  
 25 coverage. *Powers v. United Servs. Auto. Ass'n*, 114 Nev. 690, 702-703, 962 P.2d 596 (1998). The  
 26 mere fact that an insurer was incorrect in its coverage determination does not render it liable for bad  
 27 faith if its position was reasonable. *American Excess Ins. Co. v. MGM Grand Hotels*, 102 Nev. 601,  
 28 605, 729 P.2d 1352 (1986). Thus, an insured is generally required to prevail on its declaratory relief or

1 breach of contract claims regarding policy coverage as a predicate to the insurer's liability for bad faith  
 2 or on a statutory claim under NRS. 686A.310 based on a wrongful denial of coverage.

3 In this case, Plaintiffs allege that Defendant wrongfully denied coverage for the underlying  
 4 lawsuits based on inapplicable policy exclusions and that Defendant's denial of coverage was  
 5 unreasonable and made in bad faith. Plaintiffs allege that Gulf Insurance Company preliminarily  
 6 accepted coverage for some of the underlying lawsuits, but that Travelers later reversed its position and  
 7 denied coverage for substantially similar lawsuits based on various policy exclusions that were not cited  
 8 in Gulf's earlier letters.<sup>1</sup> Plaintiffs allege that the reversal of Defendant's coverage position was due to  
 9 Gulf's deteriorating financial condition and its pending merger with Travelers. The issue of whether  
 10 the policy exclusion is unambiguous as applied to the underlying lawsuits may be an issue of law that  
 11 can be resolved on motion for summary judgment. *Capitol Indemnity Corp. v. Blazer*, 51 F.Supp. 2d  
 12 1080, 1083-84 (D.Nev. 1999). Conversely, if the court decides that the policy exclusions are  
 13 ambiguous, extrinsic evidence may be admissible at trial to establish a reasonable interpretation of the  
 14 ambiguous policy provision and may also be admissible in determining whether the insurer's coverage  
 15 position was unreasonable. Certain evidence, such as reserves set by the insurer in the underlying  
 16 lawsuits or Gulf's allegedly deteriorating financial condition and its pending merger with Travelers,  
 17 will only be admissible on the issue of bad faith. Introduction of such evidence in the trial of the  
 18 coverage issue would be unduly prejudicial to Defendant. Additionally, a trial of the bad faith claims  
 19 will be unnecessary if the Defendant prevails on the coverage issue. These factors therefore favor the  
 20 bifurcation of the trial of the contractual coverage issues and the bad faith claims. *See Evanson*  
 21 *Insurance Co. v. Robb Technologies, LLC*, 2006 WL 1891134 (D.Nev. 2006) \*3.

22 There are pros and cons as to whether discovery on the bad faith issues should be bifurcated and  
 23 stayed until the insurance coverage issue is resolved. If the insurer prevails on the coverage issue by  
 24 either summary judgment or at trial, expensive and time consuming discovery on the bad faith issues  
 25 may be avoided. If the insured prevails on the coverage issues, however, the parties will then be  
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27       <sup>1</sup>Travelers' affirmative defenses set forth in its answer also appear to raise a defense to coverage  
 28 on the grounds that the underlying lawsuits are not within the scope of coverage of the insurance policy.

1 required to proceed with further discovery on the bad faith claims, resulting in two completely separate  
2 trials before different juries. In this latter regard, *Drennan v. Maryland Casualty Co.*, 366 F.Supp.2d at  
3 1008, states:

4 Joint discovery is more convenient to the parties and would further  
5 judicial economy. With joint discovery the parties will be better  
6 informed with regard to settlement efforts. Moreover, any discovery  
disputes likely will pertain to both causes of action. Finally, joint  
discovery will expedite resolution of the entire matter by permitting the  
second trial, if necessary, to commence immediately after the first.  
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8 Because joint discovery allows both phases of the case to be tried to the same jury, the second  
9 phase of the trial is also likely to be shortened because there will be no need to again present evidence  
10 from the first phase of the trial.

11 Although Defendant argues that the provisions of the policy unambiguously bar coverage for the  
12 underlying lawsuits, it has not presented any proof for this assertion in its Motion to Bifurcate. Nothing  
13 in this Order, however, precludes Defendant from promptly moving for summary judgment based on  
14 the allegedly unambiguous policy provisions. The Court can also limit the scope of coverage and bad  
15 faith discovery under the factors set forth in Fed.R.Civ.Pro. 26(b)(2) as it has done in its Order  
16 regarding Plaintiffs' Motion to Compel (#28). While this does not eliminate potentially expensive and  
17 time consuming discovery on the bad faith issues, it is a preferable method for furthering the goal of  
18 judicial economy than is an order bifurcating and staying bad faith discovery. Accordingly,

19 **IT IS HEREBY ORDERED** that Defendant The Travelers Indemnity Company's Motion to  
20 Bifurcate Bad Faith Claims, and Stay Discovery Related to Bad Faith Claims Pending Resolution of  
21 Contingent Contract Claims (#30) is **granted** in regard to trial of the breach of contract and declaratory  
22 judgment claims from the trial of Plaintiffs' insurance bad faith and statutory violations claims.  
23 Defendant's Motion (#30) to bifurcation and stay of discovery of the bad faith claims until after the  
24 resolution of the breach of contract and declaratory judgment claims is **denied**. Pursuant to this order,  
25 the parties will prepare both the insurance coverage and bad faith claims for trial. Trial of the breach of  
26 contract and declaratory judgment claims, if necessary, will first be tried and submitted to the jury. If  
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1 appropriate in light of the verdict on insurance coverage, the bad faith issues will then be tried to the  
2 same jury.

3 DATED this 4th day of February, 2008.

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5 GEORGE FOLEY, JR.  
6 United States Magistrate Judge

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